required to avoid dilution was 17.3 percent [2.16 ÷ 15.38) x (18.98 ÷ 15.38)].

Q. Have there been offerings of common stocks during 1974 by generally comparable electric and electric-gas utilities which indicate the current cost of common equity?

A. Yes. Thirty-seven underwritten offerings of common shares were made to the public during 1974 by companies in the group of 79 utilities (through November 15, 1974). The significant averages (mean) are as follows:

Ratio of current earnings to net proceeds	15.8%
Ratio of current dividends to net proceeds	11.0%
Ratio of net proceeds to book equity per share outstanding*	75%

* Average for 32 issues.

New equity capital has been available to the utilities during 1974 at prices which, after underwriting costs and company-incurred flotation costs, were typically 25 percent below book equity, representing original cost dollars committed by old investors. The dividend cost rate was typically 11.0 percent. The average dividend payout ratio was 70 percent. Retained earnings averaged 4.8 percent of net proceeds. The sum of the dividend cost rate (11.0 percent) and a 4.8 percent growth rate is 15.8 percent which, of course, is the same as the earnings net proceeds ratio. Thus, the recent offerings of common shares by electric and electric-gas utilities indicate a current cost rate in the range of 16 percent, subject to the limitations of this measure.

Q. Have you made a study to determine the extent to which the market value of the Iowa-Illinois common stock has declined relative to the common stocks of other regulated and unregulated enterprises?

A. Yes. The chart on page 42 of my exhibit shows the changing relationship between market price and book equity per share for Iowa-Illinois, the 79 electric and electric-gas utilities, the eleven food processors, and Standard & Poor's 425 industrials. Unlike the stock price indexes, these ratios account for changing amounts of book capital employed per share.

Average market price of the Iowa-Illinois stock was 2.2 times book equity in 1961, and rose to 2.7 times book equity in 1965. Since then, the loss of investor favor has been almost continuous. The price of the Iowa-Illinois stock was only 18 percent above book equity per share in 1971 and 8 percent above in 1972. Rate increases allowed Iowa-Illinois were not sufficient to reverse this trend. In the third quarter of 1974, the average price was 62 percent of average book equity per share (Exhibit, pp. 37 and 44).

In contrast, the market-to-book ratios for Standard & Poor's 425 industrials have fluctuated since 1961 above and below the 200 percent level, and declined to an estimated 129 percent under third quarter 1974 market conditions.

Q. What is your opinion of the significance of these comparative market-to-book ratios?

A. Viewed broadly, financial integrity concerns the maintenance of stock market values. It may be agreed that regulation has no obligation to allow a fair return on whatever prices investors have paid for utility stocks. It also may be agreed that financial integrity means, at a minimum, the maintenance of stock market values somewhere above book value. The crucial issue is: How much higher than book value? The recent market-to-book experience of Iowa-Illinois and most other electric utilities portends a road to financial disaster. Earnings which are no more than sufficient to maintain market prices at the book equity level reflect a regulatory standard which disregards past inflation and deprives equity investors of opportunities to realize returns commensurate with those on other investments of corresponding risk.

When earnings deficiency is still greater, so that investors consider the value of utility stocks to be substantially below the nominal dollars of previously committed capital, the regulatory process has introduced a vicious circle of cause and effect within which each successive stock offering dilutes book equities attributable to outstanding shares.

Since earnings are an allowable rate on investment, the earning power of each outstanding share is reduced by the sale of additional shares, and to compensate for this, market prices decline. The next sale of stock by the company is at a still lower price, and the downward spiral accelerates. Investor confidence is further impaired, and the current cost of new equity is pushed still higher. A practical limit to the sale of equity is reached when the market price becomes so depressed that the dividend yield equals the rate of earnings on book equity.

To maintain financial integrity, the values of the stocks of regulated companies should have some reasonable relation to the values of the stocks of unregulated companies. Stated differently, the earnings of utilities should be sufficiently high to achieve market-to-book ratios which are consistent with those prevailing for stocks in broad segments of the capital market.

Q. What are some of the differences between utilities and industrials with respect to financing under adverse market conditions?

A. Stock prices below book equity impair the financial integrity of any corporate entity, whether public utility or industrial. The effect on ability to obtain new capital from external sources is much the same for utilities and industrials. Inadequate earnings and reduced coverage of interest requirements limits the ability to raise funds through debt or preferred stock financing. Equity financing, a self-defeating exercise, is the alternative when a company can no longer sell debt or preferred stock.

The difference is that utilities do not have the same freedom as industrials to adjust financial decisions to adverse market conditions or the impact of inflation. Finance budgeting principles do not permit the sale of new securities when the effect is to reduce the well-being of the company's stockholders. Utility managements are not guided by that principle. They have an obligation to obtain the capital required to provide adequate service. It is reported that postponement or cancellation of future construction expenditures by utilities in the United States has now reached more than \$16 billion. Postponement of construction may be a wise expediency, but the dilemma can be resolved in the longer term only by higher earnings rates for common equity if the utilities' obligations to provide adequate service are to be fulfilled. Stock prices significantly below book equity are a threat to the future ability of utilities to provide adequate service by making it difficult and perhaps impossible to obtain the funds needed to finance construction. The consequences are not only adversity for stockholders, but also adverse effects on consumers and the well-being of the entire economy.

Q. Will you now describe the chart on page 45 of the exhibit?

A. The chart shows, for 75 among the 80 electric utilities (those for which data are available), the relationship between earnings on book equity for the twelve months ended June 30, 1974, and market-to-book ratios at about that date. The market-to-book ratio is the average June price divided by book equity at June 30. The diagonal line represents the relasionship between the two variables. It will be noted that only ~~six~~ 5 of the 75 companies were selling at prices above book equity.

Q. What rate of earnings on book equity is required to move the market price of the average stock to, say, 20 percent above book equity?

A. Assuming no change in market opinion from that reflected by the data shown on page 45 of the exhibit, a return of over 17 percent is required if the average company is to have a market value equal to 120 percent of book equity.

This analysis is similar to an acceptance of the present level of earnings/price ratios as a measure of the cost of capital. The average return on equity for the 75 electrics -- 10.5 percent at a market-to-book ratio of 77 percent -- corresponds to an earnings/price ratio of 13.7 percent. Under normal conditions, earnings/price ratios understate the cost of common equity, so that by this test a return of over 17 percent on book equity would be required to support a price 20 percent above book equity. However, the present level of earnings/price ratios should not be viewed as indicators of investors' long-term return requirements. If investor confidence is restored, the earnings/price ratios will decline and the market-to-book ratios will rise. In the present circumstances, the regulatory commissions face a compelling need to take action to restore investor confidence so that market prices of utility stocks will rise to levels above book equity per share.

Q. What conclusions have you drawn from these studies of the market behavior of Iowa-Illinois and other electric and electric-gas utilities?

A. I conclude that the current capitalization rate for the Iowa-Illinois stock is in the 14 to 15 percent range.

The investor's capitalization rate has increased from the 12 percent level to the 14 to 15 percent range within a span of a relatively few months. This shift reflects the combined effects of the sharply higher inflation and greater risk premiums now required by investors. There is no prospect of a decline to a return requirement of 12 percent within the foreseeable future.

In reaching this conclusion, I have accounted for the loss of investor confidence in utility stocks, the changes affecting investment risk, the inflation premium, the greater demand for capital relative to supply, the prospectively high level of interest rates, the public interest in adequate energy supplies, the leverage position of Iowa-Illinois equity, and the short-term behavior of the stock market.

The higher rate of compensation for risk-taking is required because of: higher operating expenses and obligations to make large capital expenditures, which erode earnings under existing rates; the necessity of raising new capital under unfavorable market conditions; the decline of the drawdown ratio; the lags in regulatory responses to cost pressures and, in the case of gas distributors, the uncertainty that adequate supplies will be available.

Q. May the 14 to 15 percent be taken as the current cost of common stock capital to Iowa-Illinois?

A. No. The current capitalization rate does not measure the current cost of equity capital to Iowa-Illinois. An allowance for market pressure and cost of financing must be added to the 14 to 15 percent.

I have made an allowance of 7.0 percent for market pressure and cost of financing combined. That allowance is reasonably consistent with the experience of recent years. Therefore, the estimated current cost of equity capital to Iowa-Illinois is 15 to 16 percent, representing the 14 to 15 percent capitalization rate plus one percentage point for cost of financing and market pressure.

III-4. Comparable Earnings As Evidence of Cost of Common Stock Capital to Iowa-Illinois Gas and Electric Company

Q. Please define the comparable earnings method.

A. The comparable earnings method looks to the returns earned on common equity investments, expressed in terms of original cost or book amounts, in regulated and unregulated undertakings having generally similar risks. The hypothesis is that it is reasonable to

DOCKET NO. RPU-91-6

STATE OF IOWA

DEPARTMENT OF COMMERCE

UTILITIES BOARD

IN RE: IPS ELECTRIC, A DIVISION OF IOWA PUBLIC SERVICE COMPANY	)	DOCKET NO. RPU-91-6

FINAL DECISION AND ORDER

(Issued June 1, 1992)

SYNOPSIS[1]

On August 2, 1991, the Consumer Advocate Division of the Department of Justice filed a petition pursuant to IOWA CODE § 476.3(2) (1991) requesting reduced rates for IPS Electric, a division of Iowa Public Service Company. On October 25, 1991, IPS Electric filed an application to change rates pursuant to IOWA CODE § 476.6 (1991) and provided notice to customers of proposed changes.

Several adjustments to the test year were part of a settlement agreement approved by the Board on March 13, 1992.

Adjustments to 1990 test year revenues and expenses in addition to the adjustments approved in the settlement included, but were not limited to, holding company merger costs and related merger savings and a management efficiency reward.

[1]The purpose of this synopsis is to provide readers a brief summary of the decision. While the synopsis reflects the order, it shall not be considered to limit, define, amend, or otherwise affect in any manner the body of the order including the findings of fact and conclusions of law.

APPEARANCES

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I. PROCEDURAL HISTORY

On August 2, 1991, the Consumer Advocate Division of the Department of Justice (Consumer Advocate) filed with the Utilities Board (Board) a petition asking the Board to reduce the retail rates of IPS Electric, a division of Iowa Public Service Company, so that when applied to adjusted 1990 test year sales, they would produce total Iowa jurisdictional operating revenues not in excess of $198,557,025. The Board docketed this proceeding, identified as Docket No. RPU-91-6, and established a procedural schedule on August 19, 1991. IPS Electric responded to Consumer Advocate's petition on October 25, 1991, by filing an application to change rates. Prior to that filing, IPS Electric notified its customers by a separately-mailed letter of its proposed change in rates. Intervention was granted to Mid-Size Energy Group, Inc. (Mid-Size), on August 19, 1992, and Terra International Inc. on December 18, 1991.

A "Settlement Agreement" and a "Joint Motion for Approval of Settlement Agreement" were filed on March 2, 1992. On March 6, 1992, a "Second Settlement Agreement" and a "Joint Motion for Approval of Second Settlement Agreement" were filed with the Board. A hearing on the proposed settlements was held on March 11, 1992, and a hearing on the remaining issues: merger costs, merger sharing, expenses related to the Rock Valley pilot project, and the rate of return on common equity, was held on March 11 through 13, 1992. The two proposed settlements were approved by the Board during the hearing on the contested issues. (Tr. 657-60).

The contested issues listed above were also presented to the Board in the Midwest Gas rate proceeding, Docket No. RPU-91-5. Midwest Gas is also an operating division of Iowa Public Service Company. The Board issued its decision in Docket No. RPU-91-5 on May 15, 1992. While the decisions on the contested issues in the Midwest Gas case are not binding in this proceeding, the Board finds much of the analysis applies in light of the evidence presented. To the extent that new evidence and arguments were advanced in this proceeding, the Board will address those issues.

II. TEST YEAR

The test year for the proceeding is calendar year 1990.

III. ROCK VALLEY ENERGY EFFICIENCY PROJECT

A. POST-JULY 1, 1990, EXPENDITURES

IPS Electric began developing the Rock Valley Energy Efficiency Project in 1989 in the community of Rock Valley, Iowa, a northwest Iowa community with a population of about 3,000. (Ex. 404 at Tr. 761). According to IPS Electric, the purpose of the project was to determine the impact of a coordinated offering of energy efficiency programs on a single community for use in developing its future energy efficiency programs systemwide. (Ex. 403, pp. 59-61). IPS Electric installed in Rock Valley the Metricom metering system, an advanced metering and two-way radio communications system, and in a local building established the Energy Center, a technology demonstration and education facility. (Ex. 402 at Tr. 631-32; Ex. 406).

IPS Electric proposed recovery of certain expense and capital items related to the project. (Tr. 335-38). IPS Electric argued the costs of the Energy Center and the Metricom metering system have longevity as a part of IPS Electric's operations and should be collected through general rates, rather than as energy efficiency expenditures. (Ex. 208; Ex. 407).

According to IPS Electric, the Energy Center, which now contains displays of energy efficiency equipment as well as office space for the Rock Valley project and Metricom employees, could eventually be converted to a utility service center and, therefore, its long-term usefulness is as a utility property. (Ex. 401, p. 12). In addition, IPS Electric contended the costs of the Metricom meters should recovered in utility rates, just as previous experimental metering equipment has been allowed.

Consumer Advocate asserted the energy efficiency project is of no value to customers, and customers should not be required to pay for it. (Tr. 388). According to Consumer Advocate, Rock Valley is not an appropriate test site for an energy efficiency pilot project because the population of Rock Valley is relatively small, Rock Valley customers use different amounts of electricity on a per customer basis than average IPS Electric customers, and Rock Valley residential customers' income is only 75 percent of the average IPS Electric residential customers' income. (Tr. 381-82). For these reasons, Consumer Advocate contended the potential success of any systemwide energy efficiency program cannot be predicted based on the results of the Rock Valley programs. (Tr. 386; Ex. 109; Ex. 404 at Tr. 740-41). In addition, Consumer Advocate argued the cost of the Metricom metering system was excessive and IPS Electric's characterization of the Energy Center as useful for utility service is unjustified. (Tr. 389-90).

The Board finds that the costs of the Energy Center and the Metricom metering system are energy efficiency expenditures, rather than expenditures to provide utility service. IPS Electric has consistently presented the project to the Board as an energy efficiency project. See, "Order Docketing Pilot Project," Docket No. PRP-90-3 (November 9, 1990). The title of the project is the "Rock Valley Energy Efficiency Research Project." (Ex. 403). The record shows that the Energy Center is used to display energy efficiency equipment and as office space for the project's employees. (Ex. 402 at Tr. 631-32). While it is true that the center may also be used as a customer service center in the future, that remains only a possibility. It is being used exclusively for the energy efficiency project at this time and will continue to be so used in the foreseeable future. (Ex. 403 at JWM-7). The Metricom metering system was installed on an experimental basis. There is nothing in the record which suggests the metering system will necessarily be used elsewhere in IPS Electric's service territory. At this time, the meters and the Energy Center are part of an energy efficiency pilot project and the costs of those meters should be considered as energy efficiency expenditures, pursuant to IOWA CODE § 476.6(19) (1991).

Since the expenditures related to Rock Valley are energy efficiency expenditures, the costs incurred after July 1, 1990, may be considered for approval by the Board in an IOWA CODE § 476.6(19) energy efficiency proceeding. IOWA CODE § 476.6(19)"b"(2) (1991) states, in part:

> Energy efficiency expenditures incurred on or after July 1, 1990, may be included in a utility's initial energy efficiency plan and budget submitted pursuant to paragraph "a."

In rules adopted pursuant to that Code section, the Board specified that proposed rates which contain expenditures incurred after July 1, 1990, for demand side energy efficiency programs shall not be included in a proposed tariff relating to a general increase in revenue. IOWA ADMIN.

CODE 199-7.4(4) (1992). An individual energy efficiency program should not be considered in isolation, but instead should be considered in the context of the utility's total energy efficiency plan.

IOWA ADMIN. CODE 199-35.8(10) (1992) states that pilot projects may be included as a program, in an energy efficiency plan, if justified by the utility. To ensure the Board has all the relevant information available on the pilot project, the parties in the IPS Electric and Midwest Gas energy efficiency plan approval proceeding will be required to provide the following specific information with respect to the Rock Valley pilot project:

1) To the extent available, baseline electric and gas loads for both peak and off-peak periods by customer class and community-wide prior to implementation of the project;

2) The potential energy and demand savings by program, by customer class, and on a community-wide basis; and,

3) Using incremental or full costs where appropriate, the estimated cost-effectiveness of the project using the "societal test," for individual programs and the entire project.

B. PRE-JULY 1, 1990, EXPENDITURES

The test year also contained expenses related to the Rock Valley Project incurred prior to July 1, 1990. The Board's decision with respect to the post-July 1, 1990, energy efficiency expenditures necessitates a decision with respect to those remaining test year amounts. Because of the peculiarities associated with implementing Iowa's new energy efficiency statute, the pre-July 1, 1990, energy efficiency expenditures are non-recurring. Because energy efficiency expenditures will no longer be reflected in base rates but will be eligible for recovery through the energy efficiency proceedings, they will not recur for regulatory purposes and should not be reflected in representative costs. In contrast, recovery of energy efficiency expenditures will be accomplished directly. IOWA CODE § 476.6(19) (1991). Because the amounts IPS Electric will spend on energy efficiency will become eligible for recovery through the IOWA ADMIN. CODE 199-Chapter 35 energy efficiency proceedings in the future, it is not necessary to reflect a representative amount for energy efficiency expenditures in base rates. Therefore, the expenses related to Rock Valley prior to July 1, 1990, will be disallowed.

The Board will include the pre-July 1, 1990, capital expenditures related to the Metricom meters and the Energy Center, approximately $51,583, in rate base. Both the meters and the building are currently providing service. Because these expenditures are not viewed within the context of a "representative amount analysis" and will not be considered in the subsequent cost recovery proceedings, they will be considered here for rate base purposes. Judgment on the rate base amounts incurred after July 1, 1990, will be deferred until the cost recovery proceeding.

IPS Electric does have a small, indirect ownership interest in Metricom: Midwest Resources owns 12.5 percent of UTECH and UTECH owns $2.2 million of Metricom stock. (Ex. 405 at Ex. 143, pp. 14, 21, and Ex. 150). Therefore, IPS Electric has an interest of approximately $275,000 in Metricom. Even acknowledging the alleged conflict of interest, the Board can find no prejudice on this record. Metricom was chosen after a thorough examination of other available metering systems. (Ex. 406, pp. 142-55). The costs of the Metricom system appear to be in line with the other bid received. (Ex. 405 and 406). Given the limited ownership interest Midwest Resources has in Metricom and the process engaged in to evaluate and choose the provider, this concern should not disable recovery.

IV. MERGER COSTS AND SAVINGS

A. MERGER COSTS

Iowa Resources and Midwest Energy, the holding company of IPS Electric, merged into one holding company called Midwest Resources. The merger of the holding company was reviewed by the Board in Docket No. SPU-90-5. The merger of the Midwest Resources utilities, IPS Electric and Iowa Power Inc., is currently pending before the Federal Energy Regulatory Commission (FERC), having been previously reviewed by this Board in Docket No. SPU-91-10. IPS Electric proposed to recover a total of $1,523,311 of holding company merger costs. (Ex. 202, Sch. 2, p. 2; Sch. 7; Tr. 114). A total of $1,444,190 was booked to IPS Electric in the 1990 test year. (Ex. 202, Sch. 4 and Tr. 43). IPS Electric also proposed to collect $676,535 associated with the merger of IPS Electric and Iowa Power. (Ex. 202, Schs. 3 and 7). IPS Electric proposed that those costs be collected from ratepayers over three years, at an annual amortization amount of approximately $630,314. (Ex. 202, Sch. 4). If the Board allows a time period longer than three years over which the merger costs are to be spread, IPS Electric contends it should earn a return on the unamortized amount. (Tr. 106-07).

Consumer Advocate objected to the proposals stating the costs of the merger of the holding companies are nonrecurring costs. Consumer Advocate argued the costs are expenditures made to facilitate the merger of the holding companies and are not necessary to the provision of utility service and, therefore, not properly chargeable to ratepayers. (Tr. 278). Consumer Advocate argued also that ratepayers have already paid for the consolidation of Iowa Resources' and Midwest Energy's operations. (Tr. 77, 192).

The Board will allow IPS Electric to recover the costs of the holding company merger. The subsidiaries of the new holding company, including the utilities, are the beneficiaries of the merger of the holding companies. The merger costs allocated to the utilities, therefore, are associated with the provision of utility service. In past cases, the Board has allowed other holding company costs properly allocated to IPS Electric to be included in rates. In addition, costs which are not directly related to the provision of utility service, nonetheless, may be recoverable by the utility. For example, costs such as regulatory assessments and taxes are not directly associated with the provision of utility service, but are expenses of doing business by the utility, and as such are recoverable. The merger of the holding companies was the initial step in bringing their two utilities together and allowed IPS Electric to secure the benefits of reduced costs allocated to it as a division of a subsidiary. (Ex. 202, Sch. 5). The Board finds that IPS Electric should recover the allocated portion of the costs of the merger of the holding companies.

IPS Electric also proposed to recover $676,535 over a three-year period associated with the proposed merger of IPS Electric and Iowa Power Inc. Part of this amount is actual and part is an estimate. The actual costs incurred through December 31, 1991, are $308,903, which is related to early retirement, and $135,939, which are other costs. The remainder,

$231,698, represent estimated costs. (Ex. 202, Sch. 3). The merger proposal was recently reviewed by the Board in Docket No. SPU-91-10. However, the Board will not now allow recovery of those costs. While they may be at some future time the appropriate subject for cost recovery, a portion of the numbers provided by IPS Electric are at this time only estimates of costs. The costs that are actual merger costs are also premature. The merger is not yet final. Final approval is still pending in some jurisdictions. The Board will not approve costs related to an uncompleted merger.

The parties do not dispute the fact that the holding company merger costs are one-time or nonrecurring costs. IPS Electric proposed that the costs be collected over a three-year period to reflect the average time between rate cases similar to the treatment given rate case expense. IPS Electric also pointed to the difficulty in tracking the savings as time passes and its willingness to forego a return on the unamortized balance as a basis for a three-year recovery period. (Tr. 106-08, 116-18). Consumer Advocate recommended that if cost recovery was allowed, the costs be collected over a ten-year period of time, which it asserts would better reflect the period of time the merger savings are expected to be realized. (Consumer Advocate Initial Brief, p. 7, fn. 6).

The Board does not necessarily correlate the typical three-year rate case period and recovery of rate case expenses with these merger costs. However, because recovery over a longer period as suggested by Consumer Advocate would permit IPS Electric to collect only 61.4 percent of its costs[2], the Board believes ten years is too long. Instead, the Board finds a four-year time period for recovery will reasonably balance the competing interests. The Board will not allow IPS Electric to earn a return on unamortized amounts. (See, e.g., Interstate Power Co., Docket No. RPU-86-8).

B. MERGER SAVINGS

IPS Electric proposed that any savings resulting from the merger which were in excess of the merger costs be shared equally between customers and shareholders. (Tr. 736-37, 742). IPS Electric provided testimony that the savings exceed costs by $1,784,243[3] and proposed that it be allowed to retain 50 percent of the net savings, or $892,127. (Ex. 202, Sch. 7). IPS Electric also proposed to continue to track merger related savings . (Tr. 737).

Consumer Advocate argued that the proposal would move the Board from cost-based rates and provide "monopoly" profits.[4] (Tr. 700). In addition, Consumer Advocate stated any risk of the merger was already reflected in IPS Electric's common stock price and this proposal would allow shareholders to be compensated twice. (Tr. 701). Consumer Advocate also argued consolidations should be influenced solely by the prospect of lower cost of service, not a reward above fair rates of return.

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[2]Based on a present value analysis assuming a five percent discount rate and recovery over ten years.

[3]Including both the actual holding companies merger costs and actual and estimated utility companies merger costs.

[4]Consumer Advocate provided no definition for its term "monopoly profits." The Board assumes Consumer Advocate either intended the term to mean the same as "monopoly rents" or be a hyperbolic reference to earnings above the authorized rate of return.

The Board has reviewed the savings proposal offered by IPS Electric and rejects it. The IPS Electric proposal presents unnecessary administrative complexity and would invite costly and contentious litigation since the net savings amounts would be difficult to verify on a recurring basis.

The Board will adjust expenses to reflect the substantial savings identified by IPS Electric. (Ex. 202, Sch. 5). The Board recognizes that the merger has resulted in significant savings to IPS Electric customers and commends IPS Electric for its efforts to date. Those savings will continue. As a policy matter, the Board believes it should, through its policies and procedures, encourage utility mergers and consolidations where ratepayers can benefit significantly as demonstrated here.

The statutory provision for rewarding or penalizing utilities is found in IOWA CODE § 476.52 (1991). IOWA CODE § 476.52 states, in part:

> If the Board determines in the course of a proceeding conducted under section 476.3 or 476.6 that a utility is operating in such an extraordinarily efficient manner that tangible financial benefits result to the ratepayer, the board may increase the level of profit or adjust the revenue requirement for the utility. The Board shall adopt rules for determining the level of profit or the level or the revenue requirement adjustment that would be appropriate.
>
> The board shall also adopt rules establishing a methodology for an analysis of a utility's management efficiency.

Pursuant to that Code section, the Board adopted rules which establish a methodology for analysis of a utility's efficiency. IOWA ADMIN. CODE 199-chapter 29 (1992). In addition, the rules establish an adjustment to the return on common equity as an appropriate means of adjusting the level of profit. IOWA ADMIN. CODE 199-29.4 (1992). In IOWA ADMIN. CODE 199-

29.3(1) (1992), the Board identified factors which the Board may consider when evaluating the utility. The rule states, in part:

> When evaluating a utility,the board may consider any of the factors listed in this subrule and any additional relevant information. These factors will be guidelines for evaluating a utility's efficiency or inefficiency. No single factor of group of factors will be deemed conclusive evidence of efficiency or inefficiency. In considering these factors, the board may use data collected under 29.5(476) to compare a utility, except a water utility, to other utilities providing the same service in the state.

IPS Electric witness Vorbrich provided testimony concerning management efficiency actions and practices of IPS Electric that he believed to be relevant to IOWA ADMIN. CODE 199-29.3(1). In his pre-filed testimony specifically entered into evidence at transcript page 789, witness Vorbrich cited a list of efficiencies achieved by IPS.

It is important to note that the management efficiency rules were adopted prior to any utility mergers taking place in Iowa. The benefits which flow from appropriate mergers were not specifically contemplated nor addressed as appropriate for consideration in making a management efficiency award. IOWA ADMIN. CODE 199-29.3(1)"g" does provide, however, that the Board may consider other factors the Board determines to be relevant. The rules also state:

> The reality of change, and the ability of management to anticipate and respond to those changes, greatly affect any judgment of management efficiency or inefficiency, and must be considered in establishing any rewards for efficiency or penalties for inefficiency.

The Board finds that the merger of the holding companies and the subsequent corporate restructuring reflect management's ability to anticipate and respond to change and are an important factor relevant to the Board's determination of IPS Electric's management efficiency. The record shows the merger and restructuring will result in significant tangible financial benefit to ratepayers. IPS Electric reported the savings attributable to the merger and restructuring exceed the costs of the merger of both the holding companies and the utilities by $1,784,254. (Ex. 202, Sch. 7). Although, as the Board noted earlier, a portion of these savings are estimates and some of the claimed savings may not be directly attributable to the merger, the evidence shows ratepayers will receive a tangible financial benefit because of the efforts of management to merge the holding companies and subsequently restructure their corporate activities. Tracking the savings through the use of a data base system, IPS Electric found cost savings related to the elimination of duplicate positions and through economies of scale.

Therefore, pursuant to IOWA CODE § 476.52 (1991), the Board finds IPS Electric's extraordinary management efficiency has resulted in tangible financial benefit to ratepayers. The Board finds that it is appropriate to reward IPS Electric for its management efficiency. The Board will adjust the cost of common equity upward by 30 basis points as a management efficiency reward. The upward adjusted cost of common equity will be reflected as a separate item on schedules and will not be used by IPS Electric for calculating AFUDC, in calculations for energy efficiency purposes or other regulatory purposes. The 30 basis point management efficiency award will produce approximately $600,000 prior to adjusting for income taxes or about $1 million in terms of revenue. These figures are both calculated on a total company basis. The Board believes this is a reasonable amount given the extensive salutary efforts IPS Electric has taken to benefit customers. The 30 basis points award granted IPS Electric is less than the 50 basis points granted Midwest Gas for its efforts in the merger. The number of basis points is only one element in determining the award. The other is the rate base to which it is applied. Since IPS is an electric utility, it has a substantially larger rate base than Midwest Gas. Fewer basis points applied to the larger rate base grants a comparable reward.

An additional adjustment to the merger savings adjustment needs to be made in light of this decision to award IPS Electric an amount to reflect management efficiency. IPS Electric witness Smith advanced the merger sharing proposal. (Tr. 55). He made a calculation of net benefits based on annualized merger savings and merger costs. A portion of those merger savings resulted from labor reductions. Labor savings related to the merger were also implicit in the labor adjustments, which were presented by IPS witness Heinrichs and approved in the settlement. The merger savings resulting from labor expense reduction presented by two different witnesses for two different purposes do not appear to be consistent. (Cf. Ex. 202, Sch. 5, LMS WP211, and Heinrichs Sch. T, U, AP, revised AL). Witness Heinrichs adjusted wages to include FICA, life insurance, worker's compensation, 401K, and federal state unemployment taxes, which are directly related to the labor adjustments. It appears that for purposes of computing merger savings for the sharing proposal witness Smith also loaded base wages with additional unidentifiable items. Since the Board utilizes witness Smith's computation of net benefits in its determination of tangible financial benefit for purposes of its management efficiency award, the portion of Smith's labor expense savings not already reflected in

Heinrichs' labor adjustments will be added to the non-labor savings from the merger.

V. COST OF EQUITY

The U.S. Supreme Court, in its decision in Federal Power Commission v. Hope Natural Gas Company, 320 U.S. 591, (1944), held:

> The rate-making process under the Act, i.e., the fixing of "just and reasonable" rates, involves a balancing of the investor and the consumer interests. Thus we stated in the Natural Gas Pipeline Co. Case that "regulation does not insure that the business shall produce net revenues." But such considerations aside, the investor interest has a legitimate concern with the financial integrity of the company whose rates are being regulated. From the investor or company point of view it is important that there be enough revenue not only for operating expenses but also for the capital costs of the business. These include service on the debt and the dividends on the stock. By that standard the return to the equity owner should be commensurate with returns on investments in other enterprises having corresponding risks. That return, moreover, should be sufficient to assure confidence in the financial integrity of the enterprise so as to maintain credit and attract capital.

Id. at 603 (citations omitted). Various models have been developed to estimate the return necessary to attract equity capital. In Duquesne Light Company and Pennsylvania Power Company v. David M. Barasch, 488 U.S. 299, 109 S.Ct. 609 (1989), the Supreme Court noted no one method was imposed on public utility commissions in reaching their conclusions. This Board has relied upon the discounted cash flow (DCF) model, with secondary emphasis on the risk premium model. See Iowa Southern, "Final Decision and Order," Docket No. RPU-89-7 (September 14, 1990), pp. 28-33; Iowa-American Water Company, "Final Decision and Order," Docket No. RPU-90-10 (October 21, 1991). The principles stated in those orders will be relied on by the

Board for guidance in this case regarding the cost of equity. However, the Board will make its decision based on the specific facts and arguments presented in this case.

The only component of the rate of return in dispute was the return on common equity. IPS Electric calculated a 13.0 percent cost of equity, using two methods for measuring cost of equity: 1) discounted cash flow (DCF) and 2) risk premium. In his DCF method, IPS Electric witness Vander Weide used a quarterly DCF model, with a five percent reduction to price as an adjustment for flotation costs. His main DCF results were:

a. 13.8 percent for Midwest Resources;

b. 11.7 percent for his Midwest electric group; and

c. 12.2 percent for his Midwest combination gas/electric group.

In the risk premium analysis, witness Vander Weide used a risk premium of 4.5 to 5.5 percentage points. (Tr. 483). Adding this to the most recent Moody's A-rated bond rate of 8.84 percent produced a cost of equity under the risk premium approach from 13.34 percent to 14.34 percent. (Ex. 120).

Consumer Advocate proposed an 11.3 percent cost of common equity. The proposal was based upon a DCF analysis of Midwest Resources and supported by company specific "risk premium" analyses of other Iowa-based utilities or utility holding companies. (Tr. 666-706; Ex. 125, Sch. A-E; Ex. 126, Sch. A-J). Consumer Advocate witness Habr asserted that if a continuous DCF model is applied to witness Vander Weide's utility proxy groups (Ex. 207, Sch. 2-3), an average cost of equity of 11.3 percent results for the combination proxy group and 10.8 percent results for the electric group.

Mid-Size proposed a 9.95 percent return on common equity, using the Federal Energy Regulatory Commission (FERC) DCF model in analyzing three sets of electric companies plus witness Vander Weide's two proxy groups. Mid-Size witness Dahlen's analyses did not include Midwest Resources and the estimates ranged from 9.9 percent to 10.44 percent. (Tr. 10-23; Ex. 301, Sch. 2-5).

IPS Electric is an operating division of Iowa Public Service Company, which is a wholly owned subsidiary of Midwest Resources. Only Midwest Resources' stock is publicly traded. Therefore, for its main analysis, the Board will analyze Midwest Resources. The Board will also look at the DCF analysis of proxy groups of utility companies as an initial check on the DCF analysis. As in Midwest Gas, Docket No. RPU-91-5, the Board will look at both combination electric/natural gas groups and the industry-specific (in this instant case, electric) groups as a proxy in checking the cost of equity. Finally, the Board will look at the results from risk premium analyses as another check on the DCF analysis.

A. DCF ANALYSIS

As it did in the Midwest Gas, Docket No. RPU-91-5, the Board will look at the results of both the FERC and the annually discrete DCF models. The Board will not use IPS Electric's quarterly DCF model. Both Consumer Advocate and Mid-Size appear to be correct in asserting that IPS Electric's quarterly DCF model provides for double recovery of interest on dividends already paid.

1. Dividend

Midwest Resource's most recent quarterly dividend contained in the record is $0.39 paid on a quarterly basis, or $1.56 on an annual basis. (Tr. 261, Ex. 1, Sch. 4). The Board will use the figure $1.56 in its analysis.

2. Price

IPS Electric used a simple average of the high and low stock prices for the three-month period ending August 31, 1991. The source used by IPS Electric is Standard and Poor's Stock Guide. The price is $19.75 for Midwest Resources. (Tr. 525-26). IPS Electric updated this to $19.979 for the three-month period ending February 29, 1992. (Ex. 213). Consumer Advocate used an average daily closing price for the period November 7, 1990, through June 28, 1991. The price is $19.13 for Midwest Resources, and Consumer Advocate updated that price for December 23, 1991, through March 10, 1992, to $20.035. The Board will use the most recent average of $20.035 provided by Consumer Advocate.

3. Growth Rate

IPS Electric used the August 1991 consensus analysts' estimates of future earnings per share (EPS) growth reported by Institutional Brokers' Estimate System (IBES), which is 4.83 percent for Midwest Resources. IPS Electric provided the February 1992 IBES update of 3.72 percent. (Ex. 116). Consumer Advocate proposed a growth rate of 3.1 percent, the midpoint of the 2.9 percent to 3.3 percent range it estimated. The 2.9 percent is an estimate of internal growth for Midwest Resources using a representative retention ratio. The 3.3 percent is based on Midwest Resources dividend growth rate for the nine-year period ending in 1990. (Tr. 676-77). Mid-Size used a recent Value Line estimate for the dividend growth for each of the companies he used. (Ex. 301, Sch. 3).

The Board will continue to look at both historical growth estimates and forecasted growth estimates. The historical growth rate used by the Board is 2.51 percent for Midwest Resources. This is the average of 3.485

percent, the ten-year least squares growth estimate of dividends per share, and 1.544 percent, the average of ten years internal growth. (Ex. 125, Sch. C, p. 1). However, in general, the Board believes forecasted growth rates are better predictors of future growth than historical growth rates. In his testimony at transcript page 474, IPS Electric witness Vander Weide supported his use of the IBES growth forecasts stating:

> The IBES consensus growth rates (1) are widely circulated in the financial community, (2) include the projections of reputable financial analysts who develop estimates of future EPS growth, (3) are reported on a timely basis to investors, and (4) are widely used by institutional and other investors. For these reasons, I believe these consensus estimates are unbiased estimates of the investors' expectation of each firm's long-term dividend growth prospects and, accordingly, are incorporated by investors into their return requirements. Consequently, in my opinion, they provide a sound estimate of investors' long-term dividend growth expectations.

The Board is persuaded forecasts provide the better gauge of investors' expectations of growth. (Tr. 474). In this case, that is particularly true given the necessity of hypothesizing the historical growth rates of two companies since merged.

IPS Electric also supported its position by citing a study, James Vander Weide and Willard Carleton's "Investor Growth Expectations and Stock Prices: the Analysts versus Historical Growth Extrapolation," The Journal of Portfolio Management, Spring 1988. That study showed regression results containing the consensus analysts' forecasts exceeded the regression results containing the historical growth estimates. According to witness Vander Weide, this is consistent with the hypothesis that investors use analysts' forecasts, rather than historically oriented growth calculations in making buy and sell decisions. (Tr. 475).

The Board will rely primarily on the February 1992 IBES update of 3.72 percent provided by IPS Electric in its analysis. (Ex. 116, 213).

4. Flotation Costs

IPS Electric used a five percent downward adjustment to the DCF price as an allowance for flotation costs, thereby increasing the DCF cost of equity estimated and adding 46 basis points to his cost of equity estimate for Midwest Resources. (Tr. 541). IPS Electric contended a flotation adjustment was appropriate even if common stock was not issued in the test year and believes the adjustment should apply to all common equity, including retained earnings.

Consumer Advocate argued if IPS Electric's flotation cost adjustment of 46 basis points were applied to Midwest Resources' consolidated net utility assets of about $1.5 billion, then Midwest Resources would perpetually receive flotation costs of $4,865,000 annually before taxes. Consumer Advocate further argued that the total issuance cost incurred by Midwest Energy and Iowa Resources was only $6,575,200 for the period 1957 through 1989. According to Consumer Advocate, if a flotation cost adjustment is going to be made, then a secondary market transaction cost adjustment also needs to be made.

The Board has held that a flotation adjustment may be warranted in some cases. For example, in Peoples Natural Gas Company, Docket No. RPU-86-11 (March 30, 1987), the Board accepted a flotation adjustment proposed by Consumer Advocate. An adjustment seemed especially germane when there was a recent or planned issuance of common equity, as evidenced in this case. However, as witness Vander Weide pointed out, there are issuance costs associated with all issues of common stock whether issued recently or some time ago. The issuance costs of all debt issues are recovered over the life of those issues. Unlike debt, however, stock has a perpetual life making it inappropriate to recover these costs through amortization over a definite period. Therefore, recognition should be given to the need for a carrying charge to be applied to the issuance costs.

IPS Electric is correct in arguing that the primary disagreement between IPS Electric and Consumer Advocate regards the size of, rather than the need for, a flotation adjustment. The proposed adjustments range from zero to five percent. The five percent adjustment to price used by IPS Electric is too much and does not take into account a needed secondary market transaction cost adjustment. As noted above, it is reasonable to reflect some flotation costs. The Board believes that as an alternative analysis, it is reasonable to make a two percent flotation adjustment. If a two percent adjustment is made, the result is an adjusted DCF price of $19.634 for Midwest Resources, and if no adjustment for flotation is made the price is $20.035.

5. DCF Results

Utilizing this data produces the following results for Midwest Resources:

	No flotation		2.0 % flotation	
	D/P	K	Adj. D/P	K
Annually Discrete DCF				
-Historical growth	7.98	10.49	8.14	10.65
-Forecasted growth	8.08	11.80	8.24	11.96
FERC DCF				
-Historical growth	7.88	10.39	8.04	10.55
-Forecasted growth	7.93	11.65	8.09	11.81

Utilizing updated forecasted dividend and earnings growth rates, cost of equity estimates for IPS Electric's proxy groups are as follows. (Ex. 117, 118, 213).

	No flotation		2.0 % flotation	
	D/P	K	Adj. D/P	K
Combination Group				
-Annually Discrete DCF	6.80	10.61	6.94	10.75
-FERC DCF	6.68	10.49	6.82	10.63
Electric Group				
-Annually Discrete DCF	6.78	10.31	6.92	10.45
-FERC DCF	6.67	10.20	6.80	10.33

Mid-Size provided cost of equity analysis of proxy groups using the FERC DCF model and Value Line forecasted dividend growth. The results were 10.44 percent for the combination electric/natural gas group and 9.9 to 10.6 percent for his electric groups. (Tr. 12-13; Ex. 301, Sch. 3)

B. RISK PREMIUM ANALYSIS

The Risk Premium model is based on the premise that common equity carries a higher risk than debt and, for this reason, investors require a higher expected return. According to this theory, some estimate of expected risk premium is added to the current market determined debt yield to produce an estimate of the current equity return requirement. Controversy exists on the exact form of the model and the debt rate to use, and especially on the estimate of the risk premium. The capital asset pricing model (CAPM) is a variant of the risk premium approach.

IPS Electric provided testimony that the short run risk premium may rise as interest rates fall. (Tr. 605-06). The Board understands the rationale behind this argument, and, in light of the current low interest rates, will give more weight to the upper part of the 2.5 to 3.5 percentage risk premium range it has heretofore employed.

The risk premium method used by IPS Electric is similar to the method used by the Board. See, Iowa Electric Light and Power Company, Docket No. RPU-89-9 (October 25, 1990); Iowa-American Water Company, Docket No. RPU-90-10 (October 21, 1991). The difference is in the magnitude of the risk premium itself. Using the updated 8.84 percent estimate for the yield on debt, plus adding a risk premium range of 250 to 350 basis points, supports a cost of equity estimate of about 11.34 to 12.34 percent. (Ex. 120).

As another check, the Board reviewed the recent return on equity decisions of other public utility commissions for electric utilities. (Ex. 124). The 1991 average return on equity is 12.48 percent and the last three month average of 1991 is 12.27 percent. The Board notes that it is important that decisions of other commissions not be relied upon exclusively because of the potential circular effect. However, these facts are useful as a secondary check on the Board's decision. The Supreme Court said in Federal Power Commission v. Hope Natural Gas Company, 320 U.S. 591 (1944), "the return to the equity owner should be commensurate with returns on investments in other enterprises having corresponding risks." While the return averages should not be used as the sole means of determining the return on common equity for IPS Electric, a review of the returns of other electric utilities is useful as a check of whether IPS Electric's return is commensurate with the returns of other electric utilities.

C. RETURN ON EQUITY

The DCF analyses of Midwest Resources supports a cost of equity range of 10.4 to 12.0 percent. Our preference for the forecasted growth estimates suggests the upper end of this range. DCF analysis of the combination proxy group supports a cost of equity range of 10.4 to 10.8

percent. DCF analysis of the electric proxy groups supports a cost of equity range of 9.9 to 10.6 percent. The Board's risk premium analysis suggests a range of 11.34 to 12.34 percent. While the DCF analysis remains the Board's primary approach, testimony in this proceeding raises significant doubts about its reliability in current market conditions.

Therefore, based on the various methods discussed in this order, the range is somewhere between 12.34 percent on the high side and 9.9 percent on the low side. Taking all of these methods into consideration and taking into consideration the particular facts of this case, the Board believes the proper cost of equity for IPS Electric to be in the upper range of the DCF analysis and the risk premium check. The Board finds 12.0 percent as a reasonable determination of the cost of equity. The DCF analyses, with or without the flotation adjustment, and the risk premium analysis all support 12.0 percent.

VI. FINDINGS OF FACT

Based on a thorough review of the entire record in these proceedings, the Board makes the following findings of fact:

1. The post-July 1, 1990, expenses of the Rock Valley Energy Efficiency Project are classified as energy efficiency expenditures for purposes of IOWA CODE § 476.6(19) (1991).

2. Rock Valley Energy Efficiency Project expenditures incurred on or after July 1, 1990, may be considered in an energy efficiency proceeding pursuant to IOWA CODE § 476.6(19) (1991).

3. It is unreasonable to include an amount related to pre-July 1, 1990, expenses of the Rock Valley Energy Efficiency Project as they are

non-recurring for regulatory purposes and thus not representative of prospective expenses.

4. The pre-July 1, 1990, capital expenditures related to the Metricom meters and the Energy Center are properly included in rate base.

5. It is reasonable to adjust test year expenses by one-fourth of the amount of expenses related to the merger of Iowa Resources and Midwest Energy.

6. It is unreasonable to adjust test year expenses for the expenses, both estimated and actual, related to the merger of Iowa Public Service Company and Iowa Power.

7. It is reasonable to adjust test year expenses by the amount of annualized savings related to the merger and subsequent corporate restructuring of Iowa Resources and Midwest Energy.

8. It is unreasonable to adopt IPS Electric's proposal to share the savings of the holding companies' merger.

9. IPS Electric is operating in such an extraordinarily efficient manner that tangible financial benefits result to the ratepayers.

10. It is reasonable to grant a management efficiency award in the amount of 30 basis points.

11. It is reasonable to set the return on common equity at 12 percent.

VII. CONCLUSIONS OF LAW

The Board has jurisdiction of the parties and the subject matter in this proceeding, pursuant to IOWA CODE ch. 476 (1991).

VIII. ORDERING CLAUSES

IT IS THEREFORE ORDERED:

1. The rates for IPS Electric, a division of Iowa Public Service Company, made subject to review by the filing of a petition with the Board by the Consumer Advocate Division of the Department of Justice on August 2, 1991, are declared to be excessive and unlawful.

2. On or before the expiration of 45 days from the date of this order, IPS Electric, a division of Iowa Public Service Company, shall file a revised class cost-of-service study, in both hard copy and IBM-compatible disk, and revised tariffs setting schedules of electric rates in compliance with the terms of the settlement agreements approved on March 13, 1992, the findings of this order and the summary attachments and schedules attached to and incorporated by reference. The numbers in the attachments and schedules have been rounded. The compliance tariffs shall become effective upon approval by the Board.

3. Within 60 days of the date of this order, IPS Electric shall submit for the Board's consideration and approval a plan by which refunds shall be made to customers in accordance with the findings contained herein.

4. Motions and objections not previously granted or sustained are denied or overruled. Any argument in the briefs not specifically addressed

specifically in this order is rejected either as not supported by the evidence or as not being of sufficient persuasiveness to warrant comments.

UTILITIES BOARD

Dennis J. Nagel

Nancy Shimanek Boyd

ATTEST:

Raymond K. Vawter
Executive Secretary

Emmit J. George, Jr.

Dated at Des Moines, Iowa, this 1st day of June, 1992.

STATE OF IOWA

.ERRY E. BRANSTAD, GOVERNOR

IOWA UTILITIES BOARD
DEPARTMENT OF COMMERCE

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IPS ELECTRIC, A DIVISION OF
IOWA PUBLIC SERVICE COMPANY

Docket No. RPU-91-6

"FINAL DECISION AND ORDER"

Issued June 1, 1992

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CERTIFICATE OF SERVICE

The undersigned hereby certifies that the foregoing document has been served this day upon all parties of record in this proceeding by mailing, by first class mail, to each such party a copy thereof, in properly addressed envelope with charges prepaid.

Date: 06-01-92

Walter Todd

Iowa Public Service Company
RPU-91-6
Jurisdictional Revenue Requirement

Attachment A
Final Rates

..ne No.	Description	Amount
1	Rate Base	$464,786,101
2	Rate of Return	9.933%
3	Required Return	$46,168,127
4	Less: Adjusted Income	$49,403,407
5	Income Excess	($3,235,279)
6	Income Taxes	($2,221,424)
8	Revenue Decrease	($5,456,703)
9	Plus: Adjusted Revenue	$224,999,207
10	Total Company Revenue Requirement	$219,542,504
11	Less: Non-Jurisdictional	$8,324,797
12	Plus: Deere Unit Sharing	577,000
13	JURISDICTIONAL REVENUE REQUIREMENT	$211,794,706

Iowa Public Service Company
RPU-91-6
Weighted Cost of Capital

Attachment B
Final Rates

Line No.	Description	Amount	Ratio	Rate	Weighted Cost
	(A)	(B)	(C)	(D)	(E)
1	Long-Term Debt	$308,863,353	48.805%	8.592%	4.193%
2	Preferred Equity	$65,411,863	10.336%	6.910%	0.714%
3	Common Equity	$258,576,924	40.859%	12.000%	4.903%
4	Total	$632,852,140	100.000%		9.811%
5	PLUS: Management Efficiency Award		40.859%	0.300%	0.123%
6	TOTAL RATE OF RETURN				9.933%

Iowa Public Service Company
RPU-91-6
1991 Rate Base--Electric

Attachment C
Final Rates

...ie No.	Description	Adjusted Rate Base
1	Plant in Service	$886,581,521
2	Accr. Depreciation	($329,067,573)
3	Net Plant	$557,513,949
	Deductions:	
4	Def. Income Tax	($96,769,521)
5	Pre-1971 ITC	($409,817)
6	Customer Advances	($105,439)
7	Customer Deposits	($1,103,310)
8	Accum Provisions	($396,538)
9	Allowance for Bad Debts	($297,471)
	Additions:	
10	Fuel Stocks	$13,100,693
11	Prepayments	$1,145,458
12	Cash Working Capital	($11,313,784)
13	Materials & Supplies	$3,421,882
	TOTAL RATE BASE	$464,786,101

Iowa Public Service Company
RPU-91-6
Income Statement--Electric

Attachment D
Final Rates

Line No.	Description	Adjusted Income Stmt.
	Revenues:	
1	Rate Revenue	$219,844,993
2	Other Revenue	$5,154,214
3	Total Revenue	$224,999,207
	Expenses:	
4	Fuel	$41,048,055
5	Payroll	$31,597,065
6	Other O & M	$41,150,844
7	Depreciation	$28,717,216
8	Other Taxes	$19,938,889
9	Income Taxes--Federal	$9,255,455
10	State	$2,934,950
11	Deferred	$2,552,196
12	ITC	($1,598,870)
13	Total Expenses	$175,595,800
14	OPERATING INCOME	$49,403,407

Iowa Public Service Company — Schedule 1
RPU-91-6 — Final Rates
Revenue Requirement--Electric

Line No.	Description	Total Company Amount
1	Rate Base	464,786,101
2	Rate of Return	9.933%
3	Required Return	46,168,127
4	Less: Adjusted Income	49,403,407
5	Income Excess	(3,235,279)
6	Income Taxes	(2,221,424)
8	Revenue Decrease	(5,456,703)
9	Plus: Adjusted Revenue	224,999,207
10	REVENUE REQUIREMENT	219,542,504

Iowa Public Service Company
RPU-91-6
Weighted Cost of Capital

Schedule 2
Final Rates

Line No.	Description	Amount	Ratio	Rate	Weighted Cost
	(A)	(B)	(C)	(D)	(E)
1	Long-Term Debt	308,863,353	48.805%	8.592%	4.193%
2	Preferred Equity	65,411,863	10.336%	6.910%	0.714%
3	Common Equity	258,576,924	40.859%	12.000%	4.903%
4	Total	632,852,140	100.000%		9.811%
5	PLUS: Management Efficiency Award		40.859%	0.300%	0.123%
6	TOTAL RATE OF RETURN				9.933%

Iowa Public Service Company
RPU-91-6
1991 Rate Base--Electric

Final Rates

Line No.	Description	Per Books (A)	Neal #3 Pulverizer (B)	Rock Valley Project (C)	Cash Working Capital (D)	90 Day Coal Supply (E)	Hazelton Substation (F)	Miscellaneou Workorders (G)
1	Plant in Service	872,441,290	1,601,302	42,639			1,181,816	2,463,23
2	Accr. Depreciation	(328,803,074)	(29,213)	(1,378)			(22,959)	(40,68
3	Net Plant	543,638,216	1,572,089	41,262	0	0	1,158,857	2,422,55
	Deductions:							
4	Def. Income Tax	(96,769,521)						
5	Pre-1971 ITC	(409,817)						
6	Customer Advances	(105,439)						
7	Customer Deposits	(1,103,310)						
8	Accum Provisions	(396,538)						
9	Allowance for Bad Debts	(297,471)						
	Additions:							
10	Fuel Stocks	11,872,850				1,227,843		
11	Prepayments	1,145,458						
12	Cash Working Capital	0			(11,313,784)			
13	Materials & Supplies	3,421,882						
14	TOTAL RATE BASE	460,996,310	1,572,089	41,262	(11,313,784)	1,227,843	1,158,857	2,422,55
	SOURCES:	MAH-1, Sch. A	Settlement	Ex. 208 & 407	Settlement	Settlement	Settlement	Settlement

Iowa [illegible] Service Company
[illegible]-91-6
1991 Rate Base--Electric

Line No.	Description	Payroll Capitalized	Asbestos Removal	Clean Air Act	Storm Damage	(not used)	Adjusted Rate Base
		(H)	(I)	(J)	(K)	(L)	(M)
1	Plant in Service	0	526,488	0	8,324,750		886,581,521
2	Accr. Depreciation	0	(8,555)	0	(161,708)		(329,067,573)
3	Net Plant	0	517,933	0	8,163,042	0	557,513,949
	Deductions:						
4	Def. Income Tax						(96,769,521)
5	Pre-1971 ITC						(409,817)
6	Customer Advances						(105,439)
7	Customer Deposits						(1,103,310)
8	Accum Provisions						(396,538)
9	Allowance for Bad Debts						(297,471)
	Additions:						
10	Fuel Stocks						13,100,693
11	Prepayments	0					1,145,458
12	Cash Working Capital						(11,313,784)
13	Materials & Supplies						3,421,882
14	TOTAL RATE BASE	0	517,933	0	8,163,042	0	464,786,101
SOURCES:		Settlement	Settlement	Settlement	Settlement		464,786,101

Iowa Public Service Company
RPU-91-6
Cash Working Capital--Electric

Schedule 3a
Final Rates

Line No.	Description	Revenue Days	Expense Days	Per Books	Pro Forma Adjustments	Adjusted Total	Wtd. Base Amount
	(A)	(B)	(C)	(D)	(E)	(F)	(G)
	Fuel Costs:						
1	Coal	37.71	15.72	47,618,682	(8,542,279)	39,076,403	2,354,219
2	Oil	37.71	13.92	168,384	0	168,384	10,975
3	Natural Gas	37.71	38.20	1,803,268	0	1,803,268	(2,421)
4	Union Labor	37.71	12.00	15,236,323	748,440	15,984,763	1,125,940
5	Office Labor	37.71	7.50	15,047,487	564,815	15,612,302	1,292,185
6	All Other O & M	37.71	12.47	40,568,263	987,824	41,556,087	2,873,632
7	Property Tax	37.71	364.79	17,056,493	111,069	17,167,562	(15,384,017)
8	Federal Income Tax	37.71	47.95	9,221,135	(1,632,157)	7,588,978	(212,907)
9	State Income Tax	37.71	47.96	3,066,639	(686,636)	2,380,003	(66,836)
10	FICA Taxes	37.71	10.76	1,782,929	98,726	1,881,655	138,933
11	Federal Unemploy. Tax	37.71	73.71	39,965	0	39,965	(3,942)
12	State Unemploy. Taxes	37.71	73.71	(2,665)	434	(2,231)	220
13	L-T Debt Interest	37.71	91.29	19,489,986	0	19,489,986	(2,861,023)
14	Pfd. Stock Dividends	37.71	45.46	3,324,753	0	3,324,753	(70,594)
15	Depreciation Expense	37.71	0.00	0	0	0	0
16	Pension Expense						(508,150)
17	TOTAL CASH WORKING CAPITAL						(11,313,784)

SOURCE: MAM-1, Sch. A, p. 8

Other O&M:
Total adjustments to O&M - Bulk Power + 401k & Fringes - Uncoll - I&D

Property Taxes:
Coal mill annualization + Hazelton sub + Misc. workorders • property tax adj.

FICA Taxes:
FICA tax adj. • Heal refund + Utility corrections